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No. 87-1392

In The

Supreme Court of the United States

October Term, 1987

FIRST AMERICAN NATIONAL BANK OF KNOXVILLE,

Appellant,

v.

DUDLEY TAYLOR, COMMISSIONER OF REVENUE FOR THE STATE OF TENNESSEE,

Appellee.

On Appeal From The Supreme Court of Tennessee

MOTION TO DISMISS OR AFFIRM

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16 pp

COUNTER-STATEMENT OF THE QUESTIONS PRESENTED

1. Whether the Tennessee Corporate Excise Tax, as amended in 1983, violates 31 U.S.C. § 3124(a) because the amendment was ineffective to cure the prior discrimination against Federal obligations?

2. Whether the corporate excise tax is a franchise tax or other nonproperty tax permissible within the meaning of 31 U.S.C. § 3124(a)(1)?

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COMES NOW the Appellee, Dudley Taylor, Commissioner of Revenue State of Tennessee, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, and respectfully moves that this Court dismiss the appeal, or, in the alternative, affirm the judgment below, on the grounds that it does not present a substantial federal question, the decision of the state court is in accord with applicable decisions of this Court, and there are no special or important reasons warranting briefs on the merits and oral arguments.

OPINION BELOW

The opinion of the Supreme Court of Tennessee, filed on November 23, 1987 and designated for publication, has not been reported at the time of the filing of this motion but is reproduced in the Appendix to the Jurisdictional Statement at pp. 1a to 12a.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The statement of constitutional and statutory provisions contained in the Jurisdictional Statement is adequate.

STATEMENT OF THE CASE

Dissatisfied with the Appellant's Statement of the Case, the Appellee offers the following counter-statement:

In 1983, this Court held in *Memphis Bank and Trust v. Garner,* 459 U.S. 391 (1983) that the Tennessee Bank Tax, Tenn. Code Ann. § 67-751 *et seq.,* was in violation of Rev. Stat. § 3701, as amended, 31 U.S.C. § 742 (which now appears at 31 U.S.C. § 3124(a)) because income from Federal obligations was included in the tax base while income from Tennessee bonds was excluded from the tax base. The Bank Tax was a franchise tax measured by the "net earnings" of Tennessee banks according to the definition of "net earnings" found in the Tennessee Corporate Excise Tax. After the decision in *Memphis Bank,*

the Tennessee General Assembly amended the Tennessee Corporate Excise Tax in 1983 to cure the same kind of discriminatory treatment. 1983 Tenn. Pub. Acts, Chapter 227.[1] Under the amendment, Tennessee obligations were included in the Tennessee Corporate Excise Tax base as defined in T.C.A. § 67-4-805 with the effect that both Tennessee and Federal bonds were included in the tax base on an equal basis. *Midland Bank and Trust Co. v. Olsen,* 717 S.W.2d 580, 582 (Tenn. 1986), *cert. denied,* — U.S. —, 107 S.Ct. 1336 (1987).

In this appeal, First American National Bank of Knoxville ("First American") contends that the Tennessee Corporate Excise Tax in effect for 1983 is in violation of 31 U.S.C. § 3124(a). The issues raised in the original complaint with respect to the 1982 tax payments were settled by the decision in *Midland Bank and Trust Co. v. Olsen, supra.*[2] First American claims initially that

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1. The Tennessee Bank Tax at issue in *Memphis Bank* was repealed in Chapter 227.

2. The issue presented in the appeal was first raised when First American National Bank of Knoxville ("First American") amended its complaint to allege that the Tennessee Excise Tax (T.C.A. §§ 67-4-801 through 67-4-820), as amended by the Tennessee General Assembly in 1983 in Chapter 227, Public Acts of 1983, was in violation of 31 U.S.C. § 3124. In this amendment First American sought the recovery of Corporate excise taxes paid under protest for the tax year 1983.

The original complaint challenged the Corporate Excise tax in effect in 1982. Under that taxing provision, federal bonds were included while Tennessee state and local bonds were excluded from the tax base. The issue presented for trial with respect to the 1982 taxes was the proper method for excluding the federal bond income from the excise tax base. The Trial Court ruled for First American on this issue. See Juris. Stmt. Appendix at pp. 13a to 21a. The Commissioner appealed on

(Continued on following page)

the 1983 amendment was in conflict with Tenn. Code Ann. § 9-9-112 and constituted an impairment of contract; consequently, that amendment could not cure the discrimination previously found in the excise tax. Secondly, First American claimed that the Excise Tax is not a nondiscriminatory franchise tax as permitted under 31 U.S.C. § 3124(a) and if it is, the Excise tax would not be permissible under federal law because Tennessee has another franchise tax imposed on corporations and 31 U.S.C. § 3124(a) permits only one franchise tax to be imposed by each state.

The Excise Tax is imposed by Tenn. Code Ann. § 67-4-806 on all domestic and foreign corporations for the privilege of doing business in the corporate form in Tennessee. This tax is measured by the net earnings of a corporation as defined in Tenn. Code Ann. § 67-4-805. Under this section, income from both Tennessee obligations and from Federal obligations would be included in the excise tax base.

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this issue to the Tennessee Supreme Court, however, since the identical issue was before that court in *Midland Bank and Trust Co. v. Olsen*, 717 S.W.2d 580 (Tenn. 1986), cert. denied, — U.S. —, 107 S.Ct. 1336 (1987), the Tennessee Supreme Court on the Commissioner's motion ordered that the appeal be held in abeyance pending the resolution of the appeal in *Midland Bank*.

Upon the resolution of the issues in favor of the bank in *Midland Bank*, the Commissioner refunded the 1982 taxes paid under protest by First American. The Commissioner withdrew his appeal to the Tennessee Supreme Court at which time First American assumed the role of appellant and appealed the Trial Court's decision on the 1983 taxes.

The 1982 taxes paid by First American were not an issue before the Tennessee Supreme Court.

The Trial Court held that 1983 Amendment cured the discrimination previously found in the excise tax. The Court concluded that the excise tax is a franchise tax levied on the privilege of doing business in the corporate form and does not constitute a direct tax on Tennessee obligations. Consequently, the Trial Court found that there was no impairment of contract by the amendment.

On appeal, the Tennessee Supreme Court affirmed the Trial Court's ruling that the 1983 Amendment was effective to cure the prior discrimination against federal obligations prohibited by 31 U.S.C. § 3124(a). The Tennessee Supreme Court held that the excise tax is a franchise tax imposed on the privilege of doing business in the corporate form and not on the obligations themselves. The Court also held that the 1983 amendment "does not revoke the tax immunity provided by such [Tennessee] statutes as Tenn. Code Ann. § 9-9-112." See Appendix to Juris. Stmt. at pp. 6a-7a. Accordingly, the Court held there is no infringement of the doctrine of non-impairment of contract.

The Court further ruled that the excise tax comes within the exception provided in 31 U.S.C. § 3124(a) which permits the states to include federal obligations and the income therefrom in the tax base of "nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations." The Court concluded that Congress had authorized the states to include federal obligations in the tax base of "any" nondiscriminatory franchise tax provided that this form of taxation was employed. The Court noted that Congress contemplated the taxation of federal obligations and the interest thereon under fran-

chise taxes. The Court quoted from the decision in *American Bank and Trust Co. v. Dallas County,* 463 U.S. 855, 864 (1983) as follows:

> Congress must have believed that franchise . . . taxes required federal obligations to "be considered, directly or indirectly, in the computation of the tax."

See Appendix to Juris. Stmt. at p. 10a.

The Tennessee Supreme Court rejected First American's contention that this Court abolished the distinction between an income tax "on income" and a franchise tax "measured by" income from tax exempt obligations. The court found that the franchise tax exception established by the decisions of this Court was retained in the statutory exemption as amended by Congress in 1959 and the court did not accept First American's claims that this Court indirectly abolished that distinction in *First National Bank of Atlanta v. Bartow County,* 470 U.S. 583, 594 (1985). The court rejected First American's contention that the excise tax became an income tax after the decision in *Bartow County.*

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REASONS FOR DISMISSING THE APPEAL OR IN THE ALTERNATIVE, AFFIRMING THE JUDGMENT BELOW

Since the decision of the Tennessee Supreme Court is correct and conflicts with no decision of this Court, further review by this Court is not warranted.

The Tennessee Supreme Court properly held that the 1983 amendment properly and effectively brought the Tennessee Excise Tax into compliance with 31 U.S.C. § 3124(a) and eliminated the prior discrimination against federal bonds when said amendment included Tennessee obligations in the tax base. The 1983 amendment did not revoke any immunity granted for Tennessee obligations under Tenn. Code Ann. § 9-9-112 and similar statutes. Thus, in reliance upon *Pacific Co. Ltd. v. Johnson,* 285 U.S. 480, 490 (1932), the court correctly held that the inclusion of income from state tax exempt obligations in a state franchise tax measured by net income did not violate the impairment of contract provisions in Article 1, Section 10, cl. 1, of the United States Constitution.

First American misinterprets the decision of this Court in *First National Bank of Atlanta v. Bartow County, supra,* when First American claims that this Court has abolished the possibility of a franchise tax "measured by" income from tax exempt bonds. By reading a sentence of that opinion out of context, First American attempts to manufacture a conflict with federal law which does not exist. The language in *Bartow* relied on by First Amer-

ican does not address the application of the 1959 amendment to franchise taxes but rather speaks to the application of that amendment to income taxes. 470 U.S. at 594. First American would read that opinion to say that Congress broadened the scope of the exemption to eliminate nondiscriminatory franchise taxes measured by income from the permissible forms of taxation permitted under federal law. To the contrary, *Bartow* clearly says that "The 1959 addition to § 3701 did not broaden the scope of the exemption required by § 3701 beyond that mandated by the Constitution." 470 U.S. at 593. The decision in *Bartow* acknowledges the franchise tax exception and does not reverse or limit the reading of § 3701 in *American Bank and Trust Co. v. Dallas County,* 463 U.S. at 864 which notes that Congress obviously contemplated that federal bonds would be subject to nondiscriminatory state franchise taxes.

The Tennessee Supreme Court also correctly held that the Tennessee Excise Tax is a "nondiscriminatory franchise tax or other nonproperty tax" permitted under 31 U.S.C. § 3124(a). First American suggests that the decision conflicts with 31 U.S.C. § 3124(a) by claiming that this section as "amended" in 1982 was intended to limit the states to one nondiscriminatory franchise tax which includes federal obligations. The language of this section, however, does not contain this limitation claimed by First American. This section permits any franchise tax which comes within this form of taxation. Contrary to First American's claim, the purpose of Pub. L. 97-258, 96 Stat. 877, as enacted in 1982 was to restate 31 U.S.C. § 742 and other laws related to money and finance in "simple language" and "without substantive change" and to enact those laws as title 31 United States Code. See

House Report 97-651 reprinted in [1982] U.S. CODE CONG. AND AD. NEWS 1895. Previously, Rev. Stat. § 3701, as amended, 31 U.S.C. § 742, provided the exception to that exemption in the following language: "nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations." This language as it originally appeared in the 1959 amendment imposes no limitation on the number of "franchise taxes" permitted by each state. The House Report indicates that the intention of the 1982 restatement of this section was to preserve the congressional intent of the 1959 amendment without substantive change.[3]

Finally, the Tennessee Supreme Court correctly held that the Tennessee Excise Tax which is measured by net earnings is a permissible nondiscriminatory franchise tax or other nonproperty tax under the terms of 31 U.S.C. § 3124(a). It has been settled law for many years that nondiscriminatory franchise taxes may include federal obligations in the measure of such taxes. In *Werner Machine Co. v. Director of Div. of Taxation*, 350 U.S. 492,

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3. House Report 97-651 reprinted at [1982] U.S. Code Cong. and Ad. News 1895, 1897 states:

> Substantive Changes not made.—As in other codifications undertaken to enact into positive law all titles of the United States Code, this bill makes no substantive change in the law. It is sometimes feared that mere changes in terminology and style will result in changes in substance or impair the precedent value of earlier judicial decisions and other interpretations. This fear might have some weight if this were the usual kind of amendatory legislation where it can be inferred that a change of language is intended to change substance. In a codification law, however, the courts uphold the contrary presumption: the law is to remain substantively unchanged. [Citations omitted.]

494 (1955), this Court rejected a taxpayer's contention a franchise tax must fall because it had the effect of being imposed directly on tax-exempt federal obligations. This Court stated:

> This Court has consistently upheld franchise taxes measured by a yardstick which includes tax-exempt *income* or property, even though a part of the economic impact of the tax may be said to bear indirectly upon such *income* or property. (Citations omitted)

(Emphasis added.)

There is no indication in the legislative history of the 1959 amendment that Congress intended to prohibit franchise taxes measured by income. Rather, the indication is that Congress intended to preserve the exception for nondiscriminatory franchise taxes previously recognized by the decisions of this Court. The Tennessee Supreme Court correctly rejected First American's claim that this Court in *First National Bank of Atlanta v. Bartow County, supra* abolished the exception for nondiscriminatory franchise taxes measured by income and *sub silento* overruled *Werner Machine* and other decisions which have upheld nondiscriminatory franchise taxes measured by net earnings.

The Tennessee Supreme Court's decision is in accord with the applicable decisions of this Court and there are no special or important reasons warranting briefs on the merits and oral arguments in this matter.

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CONCLUSION

This appeal should be dismissed or, in the alternative, the judgment below should be affirmed.

Respectfully submitted,

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